Frankfurt am Main,
4 September 2020

BVI[1] Position on the EBA's Consultation Paper (EBA/CP/2020/09) on Draft Regulatory Technical Standards on criteria to identify categories of staff whose professional activities have a material impact on an investment firm's risk profile or assets it manages under Directive (IFD) 2019/2034 of the European Parliament and of the Council on the prudential supervision of investment firms

We take the opportunity to present our views on the fourth consultation paper of the EBA related to **remuneration** and the Draft Regulatory Technical Standard (Draft RTS) **on criteria to identify categories of staff** whose professional activities have a material impact on an investment firm's risk profile or assets it manages under the IFD.

As a general comment, we urge the EBA to fundamentally revise its proposal on a Draft RTS on criteria to identify categories of staff and to better calibrate the criteria by fully reflecting the different business models of investment firms and the principal based approach outlined by ESMA in its remuneration guidelines due to the following reasons:

- **First, we strongly disagree that the EBA follows only the approach taken under the remuneration framework of the CRD V applicable for (inter alia systemically relevant) banks.** The suggested Draft RTS on criteria to identify categories of staff of investment firms is largely identical with EBA's proposal in its final report on a Draft RTS as per a mandate acc. to Article 94(2) CRD V on criteria to define managerial responsibility and control functions, a material business unit and a significant impact on its risk profile, and categories of staff whose professional activities have a material impact on an institution's risk profile. This approach ignores the fact that different legal bases and rationales exist under the IFD and CRD V. One of the essential differences in this respect is that the CRD V explicitly distinguishes on Level 1 between ***qualitative and quantitative criterion*** to identify categories of staff. According to Article 92(3)(c) CRD V, categories of staff whose professional activities have a material impact on the institution's risk profile shall include staff members entitled to significant remuneration in the preceding financial year (staff member's remuneration is equal or greater than EUR 500 000 and the staff member performs the professional activity within a material business unit and the activity is of a kind that has a significant impact on the relevant business unit's risk profile). These requirements do not apply under the IFD remuneration framework. This is also not an editorial mistake by the legislator of the IFD at Level 1, because the IFD was adopted at the same time as the new remuneration rules under CRD V. Therefore, if the legislator had wanted comparable quantitative rules with fixed quantitative remuneration limits to apply in the IFD as well, it would have arranged for this accordingly. **We therefore strongly disagree to shift fixed quantitative criteria applying for (inter alia systemically relevant) banks to investment firms on Level 2 for which such rules are not envisaged at Level 1 at all.**

- **Second, we urge the EBA to take due account of the Commission's Recommendation 2009/384/EC and the existing remuneration guidelines pursuant to Directives 2009/65/EC (UCITS Directive), 2011/61/EU (AIFMD) and (2014/65/EU).** We are very concerned that the EBA

[1] BVI represents the interests of the German fund industry at national and international level. The association promotes sensible regulation of the fund business as well as fair competition vis-à-vis policy makers and regulators. Asset Managers act as trustees in the sole interest of the investor and are subject to strict regulation. Funds match funding investors and the capital demands of companies and governments, thus fulfilling an important macro-economic function. BVI's 114 members manage assets more than 3 trillion euros for retail investors, insurance companies, pension and retirement schemes, banks, churches and foundations. With a share of 23%, Germany represents the largest fund market in the EU. BVI's ID number in the EU Transparency Register is 96816064173-47. For more information, please visit www.bvi.de/en.

remains silent in its consultation paper about whether and how these ESMA guidelines are considered. Attention should be drawn to subparagraph 1, sentence 2 of Article 30(4) IFD, which assigns to ESMA an active participating and guiding role in drafting the RTS, which yet is to be integrated. Moreover, the argument presented by the EBA at the hearing that approaches of guidelines could not be transferred into an RTS is not convincing. This ignores the clear mandate given in Article 30(4) IFD which (in contrast to the mandate under Article 94(2) CRD) explicitly mentions that the RTS shall be developed by EBA **in consultation with ESMA** and that the EBA **and** ESMA shall take due account these guidelines as well as aim to minimise divergence from existing provisions.

This applies even more as investment firms such as portfolio managers without a licence to hold client money or to deal on own account (investment firms defined under Article 4(1)(2)(c) CRR of the current regime) do not qualify as institutions. Until the coming into force of the IFD, they are (and have been) out of scope of the remuneration rules of the CRD IV and V and they are not required to identify risk takers (also under German law), not even where they are part of a banking group. The IFD framework lays down new rules for them for the first time regarding the identification of risk takers and the pay-out rules which requires considerable implementation (insofar as they are classified as category 2). Therefore, the argument presented by the EBA in its hearing that many investment firms are already part of a banking group and that the CRD rules should apply in a comparable manner in avoiding additional implementation effort is not convincing for these firms. This applies even more as the EBA is proposing the most stringent remuneration regime of (inter alia significant) banks for them in disregard of the principal-based approaches in ESMA's remuneration guidelines under the MiFID framework which already cover the main principles of identifying risk takers of investment firms (including portfolio managers) as well as ESMA's remuneration guidelines for asset managers under the AIFMD or UCITS directive which provide comparable business models like portfolio managers. The adherence to banking rules also for investment firms is not only inconsistent with the IFD's explicit rationale to address the specific vulnerabilities and risks inherent to (esp. category 2 and 3) investment firms by means of effective, appropriate and proportionate prudential arrangements, as the CRD only partially and therefore not adequately addresses these (ref. Recital (2) of the IFD). It will also lead to the great danger of further fragmentation of the remuneration system in the EU for undertakings which provide heterogeneous business models such as asset managers and portfolio managers. This was not the intention of the European legislator and the reason for the mandate given to the EBA in Article 30(4) IFD to take due account ESMA's remuneration guidelines.

- **Third, the banking approach is not designed to properly consider the specificities of different business models of investment firms and the characteristic risk associated to their categories of staff.** The EBA itself stated in its previously published announcements on the IFD framework[2] that '*other than the largest 'bank-like' proprietary trading firms, most investment firms commonly have different risk profiles, based on differing investor bases, risk appetites and risk horizons. Similarly, business models and structures typically vary from those in large banks, and correspondingly investment firms can have different pay structures.*' However, the proposed rigid framework of inflexible criteria does not fulfil this approach and the purposes of the European legislator. This applies entirely to the to the proposed ***quantitative criteria*** on identifying staff which should apply in any case for all staff members named in Article 6, especially paragraph (1)(a) to (c), of the Draft RTS irrespective of whether the professional activities of these staff members have a material

[2] Cf. EBA Report on investment firms, EBA/Op/2015/20, page 78; EBA discussion paper, Designing a new prudential regime for investment firms, EBA/DP/2016/02, page 57.

impact on the profile of the investment firm or the assets that it manages. Moreover, the proposed ***qualitative criteria pursuant to Article 5(4), (7) second alternative, (8) and (9) of the Draft RTSD*** do not distinguish between the fact of whether the professional activities have **a material impact on the profile of the investment firm or the assets that it manages**. In our view, it is not appropriate that the same approach for identifying staff members with material impact on the profile of the investment firm should be applicable for staff members with a material impact of the assets that it manages. Particularly in cases where the investment firm is not dealing on its own balance sheet like portfolio managers, the criteria must be formulated differently and be based on the similar principle-based requirements of the AIFMD and UCITS Directive specified by ESMA in its remuneration guidelines for asset managers.

Subject to our general comments, we would like to comment on the detailed questions as follows:

Question 1*: Are the definitions in Article 1-3 sufficiently clear?*

The definitions are clear.

Question 2: *Is the Article 4 on the application of criteria appropriate and sufficiently clear?*

- **Scope (paragraph 1)**: In principle, the mandate given to the EBA in Article 30(4) IFD is focussed on developing Draft RTS to specify appropriate criteria to identify the categories of staff whose professional activities have a material impact on the risk profile to the investment firm. It does not include the material impact on the assets that an investment firm manages. However, the general requirements of Article 30(1) IFD also include that topic. It is therefore in principle appropriate to provide clarity in the Draft RTS for these cases as well.

  However, as mentioned in our general remarks, we see the need to apply a different approach for investment firms with a licence to provide portfolio management to cover their processes for identifying staff members with a material impact on the assets managed. In particular, we see multiple interactions especially in the remuneration rules introduced under different pieces of EU law which overall amount to a huge practical burden for the affected market participants. In proposing yet another approach, investment firms providing portfolio management would be required to comply with different sets of rules regarding remuneration of their personnel at the same time: the RTS under the IFD, the ESMA guidelines under the MiFID and contractual provisions (such as provisions to fulfil the AIFMD and UCITS remuneration requirements in case of delegation of portfolio management of investment funds to investment firms). Applying all these rules required under different, unaligned regulatory regimes within one employment contract is barely possible. Since the services provided by investment firms are comparable to the services provided by management companies within the meaning of the AIFMD or UCITS Directive, it is important that also an equal remuneration regime applies to these investment firms. **In avoiding further fragmentation of remuneration systems and in considering the aim of the EU legislator to minimise divergence from existing provisions (Article 30(4) IFD), the criteria to identify categories of staff of investment firms providing portfolio management should be based on the similar principle-based requirements of the AIFMD and UCITS Directive specified by ESMA in its remuneration guidelines for asset managers. We therefore urge the EBA to add (at least) an exemption in the Draft RTS for investment firms with a licence to provide portfolio management services to align the process for identifying staff members as it is required in the ESMA guidelines.**

The EBA itself was proposing such an approach in its Annex to the EBA Opinion (EBA-OP-2017-11) in response to the European Commission's call for advice of 13 June 2016 (29 September 2017) under paragraph 340 as follows:

> *"If additional remuneration requirements (i.e. in addition to applicable requirements set in MiFID II) were* ***set for such Class 2 or 3 investment firms, they could be similar to the requirements included within CRD or similar to the requirements set in Directive 2009/65/EU (UCITS) or Directive 2011/61/EU (AIFMD) and should apply to staff having a material impact on the firm risk profile.*** *In this respect, it must be noted that only the CRD includes a limitation of the ratio between the variable and the fixed remuneration to 100% (200% with shareholders' approval).* ***The principle of proportionality should be taken into account****."*

An approach 'similar to the requirements included within the CRD' would mean for investment firms providing portfolio management without a licence to deal on own account that the remuneration rules would **not apply** for them because they are out of scope of the remuneration requirements of the CRD: they do not qualify as institutions within the meaning of the current CRR/CRD which limits the remuneration requirements to institutions. However, since the European legislator has adopted a different interpretation in the IFD framework, namely that these investment firms (category 2 firms) must in principle also draw up a remuneration policy and identify risk takers on a proportional basis, a comparable approach to that under the AIFMD or UCITS Directive must be found. The imperative nature of this approach is expressly stipulated in Art. 30(4) IFD through the inclusion of ESMA in and the specifications of EBA's mandate thereunder.

In this context, we would like to draw EBA's attention to the fact that the implementation of the proposed processes to identify staff members will increase costs and the administrative burden for investment firms which are currently not covered by the remuneration requirements to identify staff as follows:

- Adjusting the content of the remuneration policies (such as changing the scope of the remuneration policy regarding to the identified staff and the pay-out process)
- Implementation of a pay-out process for parts of the variable remuneration (such as deferral arrangements, pay-out in instruments, application of malus) including software adaption for the pay-out process and adjusting the accounting systems (such as implementation of different payment methods and new employees' accounts, monitoring of the deferral arrangements, initiation of subsequent payments)
- In cases where a pay-out process is partially in place, changing the implemented processes for salary payments of the identified staff (such as changing the calculation process for the deferred part of the bonus and the timeline of the deferred period)
- Adjusting the employment contracts of the identified staff, including conduct of negotiations with the employees
- Informing – where applicable - the workers' council ("Betriebsrat") and requiring the consent of the workers' council (including complying with the requirements of the Equal Treatment Law); in practice, there are open questions what happens if the workers' council fails to give its approval under employment legislation or collective agreements (e.g. consent for malus agreements).
- Clarification of legal issues by internal/external lawyers
- Hiring external service providers for the implementation of the new (complex) requirements.

.BVI

- **Quantitative and qualitative criteria (paragraph 2**): As mentioned in our general remarks, we strongly disagree with the proposed approach to define **quantitative criteria** to identify categories of staff of non-systemic investment firms in absence of a legal obligation on Level 1 in the IFD. In comparison to the legal requirements for banks under CRD V, the IFD does not requires that staff members entitled to significant remuneration should be identified as categories of staff whose professional activities have a material impact on the institution's risk profile. We also refer to our general remarks and our answers to question 4 regarding the qualitative criteria.

- **Group approach (paragraph 3 and 4):** We refer to our aforementioned remarks to the quantitative and qualitative criteria. We have the same concerns to apply these criteria on consolidated basis.

  Furthermore, we miss a similar group approach on Level 1 of the IFD as it is stated under the new banking regime (Article 109 CRD V) with exemptions for group entities with sector specific requirements such as UCITS or AIF management companies. The reason for this is that these exemptions under Article 109 CRD V were part of the trilogue at a very late stage of the CRD V package without a chance to involve this as a comparable rule under the IFD framework. **In view of a level playing field adequately addressing the rationale for proportionality as expressed in Recital 2 of the IFD between category 1 firms on one hand and category 2 firms on the other, we request EBA to support such exemptions also under the IFD framework (for instance as a general comment in its final report or as proposal in its Draft RTS)**.

Question 3: *What would be the appropriate percentage of own funds to determine that a business unit has a material impact on the risk profile of the investment firm? It would be most helpful if respondents could provide a quantitative estimation of the number of staff identified under this criterion at the indicated percentages in addition to the other qualitative criteria within the draft RTS as well as the cost for the application of that criterion.*

We disagree to implement a qualitative criterion which refers to staff members which have managerial responsibility for a business unit that contributes a percentage amount of the investment firm's total own funds requirements. This approach results solely from the requirements of the CRD (Article 92(3)(c)) covering staff members entitled to significant remuneration in the preceding financial year, which are not required under the IFD.

Moreover, from a practical point of view, the management responsibility for a business unit should be measured against its capital requirements. That is not a suitable approach for investment firms which calculate their own capital requirements based on fixed overheads. Own capital figures are generally not broken down by business unit based on fixed costs or K-factors. This would therefore lead to a considerable additional administrative burden if the own capital figures only had to be broken down by business units for the purpose of staff categorisation. It would also significantly limit the investment firm's ability to adjust its set-up and structure and thus adapt to changing market or strategic demands, and thus bear the potential of an additional regulatory law induced risk.

Finally, the approach taken in the Draft RTS lacks the element of proportionality as not all investment firms will feature a structure where business units significantly differ and the level of risk for the firm can be broken down by meaningful metrics.

BVI

Question 4*: Are the qualitative criteria within Article 5 appropriate and sufficiently clear?*

As mentioned in our general remarks, we disagree with the general approach that the proposed qualitative criteria on identifying staff should apply in any case for all staff members named in Article 5(4), (7) second alternative, (8) and (9) of the Draft RTS irrespective of whether the professional activities of these staff members have a material impact on the profile of the investment firm or the assets that it manages. These qualitative criteria should only be stated as examples in the Draft RTS. The investment firms should be required to assess at least itself if and to what extent the named categories of staff have a material impact on the risk profile of the investment firm or assets it manages.

This applies even more as the qualitative criteria seem very far-reaching without considering if and to what content the staff members have a material impact on the firm's risk profile or asset it manages. The pure managerial responsibility should not be enough to be identified staff. In particular, the differentiation in Art. 5(8) of the Draft RTS according to different areas of responsibility can lead to difficulties in practice with regard to the management of outsourcing agreements of critical/important functions. It is also unclear what is meant by management responsibility in terms of "performing economic analysis", especially as opposed to portfolio management.

Moreover, the MiFID services listed in paragraph 8 do not correspond to the terms used in the MiFID, which may lead to difficulties of delimitation.

The automatic inclusion of voting members of a committee with decision-making or blocking powers on new products (cf. Art. 5(9) of the Draft RTS) is considered by our members to be too far-reaching.

Question 5: *Are the qualitative [quantitative] criteria within Article 6 appropriate and sufficiently clear?*

We strongly disagree to implement quantitative criteria in the Draft RTS because it is not required on Level 1 and does not consider the different risk profiles of investment firms, based on differing investor bases, risk appetites and risk horizons. Their business models and structures typically vary from those in large banks, and correspondingly investment firms have different pay structures in practice. As mentioned in our general comments and our answers to the other questions, **the E*BA should be guided by the principal based remuneration requirements stated by ESMA in its guidelines under the MiFID, AIFMD and UCITS Directive, for which no quantitative criteria exist and also the qualitative criteria are explicitly subject to the provision that staff members have a material influence on the risk profile of the company or the managed portfolios. Alternatively, where quantitative criteria are considered relevant, these should – in alignment with the scope of section (2) of Annex II of AIFMD and Article 14a(3) of UCITS Directive – be limited to employees within the remuneration bracket defined under Article 6(1)(d) of the Draft RTS, and consequently Article 6(1)(a) to (c) should be deleted from the Draft RTS.***

****